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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION SEVEN

FIRST FEDERAL BANK OF  
CALIFORNIA,

Plaintiff and Respondent,

v.

STEPHEN M. BLANCHARD,

Defendant and Appellant.

B136268

(Los Angeles County  
Super. Ct. No. BC 105952)

APPEAL from a judgment of the Superior Court of the County of Los Angeles.

Patricia L. Collins, Judge. Affirmed.

Knapp, Petersen & Clarke, Steven Ray Garcia and Stephen M. Harris; Davis Wright Tremaine and Gary L. Bostwick, for Defendant and Appellant Stephen M. Blanchard.

Epport & Richman, Mark Robbins and Victor R. Berwin for Plaintiff and Respondent First Federal Bank of California.

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## **SUMMARY**

This is an appeal by Stephen Blanchard from a deficiency judgment entered against him in a bitterly litigated judicial foreclosure proceeding. The judgment was entered more than three years after the property was sold to the lender pursuant to an interlocutory decree of foreclosure. The foreclosure decree determined that Blanchard had defaulted on a loan from First Federal Bank of California, and declared Blanchard personally liable for payment of the debt and attorneys' fees, less the fair value of the property.

Blanchard claims the trial court erred in determining that First Federal was the prevailing party in the foreclosure proceeding. He argues that he is the prevailing party, and is entitled to attorneys' fees, because the indebtedness on the date of the foreclosure sale, exclusive of attorneys' fees and costs, was less than the fair value of the property on that date. As a result, Blanchard asserts no deficiency existed. We reject Blanchard's contentions and conclude attorneys' fees and costs were properly included in the calculation of the deficiency judgment.

## **FACTUAL, PROCEDURAL AND LEGAL BACKGROUND**

In June 1990, Stephen Blanchard entered into a loan transaction with First Federal Bank of California. Blanchard executed a note for \$630,000 and used the funds to refinance real property, which he held as an investment, located at 523 Ocean Front Walk in Venice.<sup>1</sup> The loan was secured by a deed of trust and assignment of rents on the property. The note and the deed of trust contained provisions for the award of attorneys' fees.<sup>2</sup>

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<sup>1</sup> Other loans on properties owned by Blanchard at 511 and 517 Ocean Front Walk in Venice were the subject of a separate lawsuit Blanchard brought against First Federal, in which Blanchard obtained a jury verdict on some of his claims against the bank.

<sup>2</sup> Paragraph (9) of the deed of trust provided: "If Borrower fails to perform the covenants and agreements contained in this Deed of Trust ... then Lender at Lender's option may make such appearances, disburse such sums and take such action as Lender deemed necessary, in its sole discretion, to protect Lender's interest, including, but not limited to, (i) disbursement of attorneys' fees .... Any amounts disbursed by Lender pursuant to this paragraph 9, with interest thereon, shall become additional indebtedness of Borrower secured by this Deed of Trust." (Footnote continues on next page.)

Blanchard defaulted on his loan payments. First Federal accelerated the loan, and on May 31, 1994, initiated judicial foreclosure proceedings. On January 9, 1995, Blanchard orally offered First Federal a deed to the property in lieu of foreclosure, but First Federal refused the offer and proceeded through judicial foreclosure.

In a judicial foreclosure, the secured creditor brings an action to have the court determine the loan is in default, order the security sold to satisfy the loan balance, declare the debtor liable for any deficiency arising from an insufficient sale price, and enter a deficiency judgment. (Bernhardt, Cal. Mortgage and Deed of Trust Practice (Cont.Ed.Bar 3d ed. 2001) § 3.1, pp. 134.1-135.) The principal reason a secured creditor chooses to foreclose judicially, rather than through a non-judicial trustee's sale, is to obtain a deficiency judgment. (*Id.*, § 3.4, p. 137.) First Federal's purpose in pursuing judicial foreclosure, rather than accepting Blanchard's offer of a deed in lieu of foreclosure, was to reserve its deficiency rights.

On September 6, 1995, the trial court (Judge Richard Neidorf) granted summary judgment to First Federal, ruling that (a) Blanchard owed \$704,599.02 plus subsequently accruing advances, costs and fees, "as well as past and future attorneys' fees to be determined after entry of the final judgment"; (b) First Federal was entitled to an order for the issuance of a writ of sale and to the appointment of a receiver; and (c) First Federal was entitled to a deficiency judgment, the amount of which would be determined after the sale. On October 10, 1995, an amended order for the issuance of a writ of sale was filed containing an interlocutory decree of foreclosure.<sup>3</sup>

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In his promissory note, Blanchard stated: "If the Note Holder has required me to pay immediately in full as described above, the Note Holder will have the right to be paid back by me for all of its costs and expenses in enforcing this Note to the extent not prohibited by applicable law. Such expenses include, for example, reasonable attorneys' fees."

<sup>3</sup> The decree states that a final judgment will be entered after the sale; the final judgment will be based on "the amount of indebtedness at the time of the foreclosure sale;" the indebtedness as of June 1, 1995 was \$687,295.20 and the deed of trust constituted a lien on the property for that sum, "plus all interest and costs and fees expended by First Federal for taxes, insurance, allowed costs of maintenance, management, improvement, and

The foreclosure sale was held on June 12, 1996. First Federal purchased the property with a partial credit bid of \$560,000. First Federal then filed a motion for a determination of the fair value and the entry of a deficiency judgment, as permitted by statute.<sup>4</sup> “Fair value” is the process of valuation that controls the calculation of a claimed deficiency. (*San Paolo U.S. Holding Co., Inc. v. 816 South Figueroa Co.* (1998) 62 Cal.App.4th 1010, 1022; Code Civ. Proc. § 726.) The fair value limitation prevents the creditor from obtaining a deficiency judgment for the difference between the indebtedness and the amount realized from the foreclosure sale, if the sale price was not equivalent to the fair value. (*San Paolo U.S. Holding Co., supra*, 62 Cal.App.4th at p. 1023.) First Federal’s motion asserted it suffered a deficiency at the foreclosure sale of \$197,971.72, the difference between the debt as of June 12, 1996 (\$757,971.72) and the value of the property (\$560,000), plus interest from the date of foreclosure and attorneys’ fees and costs “to be requested in a separate motion.”

A hearing to determine the fair value of the property was held on September 16, 1996, before Judge Richard G. Harris. At the fair value hearing, First Federal submitted an appraisal of \$560,000, the amount of its bid. Blanchard submitted two appraisals, one for \$815,000 and another for an even higher amount. The appraisal submitted by First Federal failed to consider the recent sale of a comparable property on Ocean Front Walk, situated only 100 yards away from Blanchard’s property. The court concluded the most comparable sale was the Ocean Front Walk sale, reflected in the appraisals submitted by Blanchard, and the fair value of the property as of the date of its sale was \$815,000.

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attorneys’ fees and costs (the ‘Subject Debt’)); and First Federal “may add attorneys’ fees to the money judgment after entry of the final judgment.” The decree further provides that Blanchard “shall be personally liable for payment of the Subject Debt and attorneys’ fees less the fair value of the property as determined at the Fair Value Hearing,” and that the court “retains jurisdiction to determine the amount of said deficiency, if any, and render a money Judgment ....”

<sup>4</sup> To seek a deficiency, the plaintiff must file an application for a fair value hearing within three months of the date of the foreclosure sale. (Code Civ. Proc. § 726, subd. (b).)

First Federal moved for reconsideration, but Judge Harris denied the motion on October 18, 1996, confirming the fair value of the property at \$815,000. At the hearing, the court indicated that a motion and ruling on the amount of First Federal's reasonable attorneys' fees and costs would be necessary. The fees and costs would then be added to the arrearage, "and, taken together, we'll know whether or not there's a deficiency when applied against \$815,000."

On November 11, 1996, First Federal filed an appeal from the court's rulings. Blanchard filed a motion to dismiss the appeal. This court granted that motion on July 22, 1997, dismissing the appeal as having been taken from a non-appealable order. First Federal's petition for rehearing was denied on August 14, 1997.

Meanwhile, six months after denial of its motion for reconsideration, on April 18, 1997, First Federal filed its motion for an award of attorneys' fees and costs. First Federal sought \$94,432.50 for fees through October 20, 1996, plus an additional \$2,550 as compensation for the fee motion, for a total fee award of \$96,982.50, plus costs of \$1,018.55. First Federal requested entry of judgment in its favor in the amount of \$40,972.77, the difference between the outstanding debt at the time of sale (\$757,971.72) plus the attorneys' fees, and the fair value of \$815,000.

Blanchard then conducted discovery on the attorneys' fees claimed by First Federal.<sup>5</sup> After discovery was concluded—two years later—First Federal filed an ex parte application to set a hearing date on its motion, and sought an additional \$111,029.91 (\$90,773.25 in fees and \$20,256.66 in costs), for a total of \$205,462.41. The additional fees covered the period December 1996 through March 1999.

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<sup>5</sup> During this time, on June 11, 1997, Blanchard redeemed the property under the provisions of section 729.060 of the Code of Civil Procedure by tendering the sale price of \$560,000 plus interest. First Federal resisted Blanchard's efforts to redeem the property, claiming that it could not be compelled to enter into the escrow arrangements Blanchard wanted to facilitate the redemption. The court (Judge Robert M. Letteau) ultimately entered an order compelling the First Federal to submit necessary documents into escrow.

A hearing was calendared for June 15, 1999. On June 8, 1999, Blanchard filed a motion to tax costs, which also served as his opposition to First Federal's motion for fees. Blanchard argued First Federal was not the prevailing party and thus not authorized to seek attorneys' fees. He also argued that, even if First Federal were entitled to recover fees, it could not obtain fees for a number of categories claimed, such as fees incurred after Blanchard offered First Federal a deed to the property in lieu of foreclosure, and fees incurred in preparing and defending its cost bill, including discovery.<sup>6</sup>

On June 23, 1999, the court (Judge Patricia Collins) referred the matter to a referee for "determination of all matters relating to attorneys' fees and costs." The parties agreed to the appointment of retired Justice Robert Feinerman as the referee. After consideration of the evidence submitted by the parties and written and oral arguments, the referee determined that First Federal was the prevailing party and was entitled to recover reasonable attorneys' fees and costs. He recommended the sum of \$151,296.90, reducing the costs requested by \$17,563.31, and deleting \$36,602 from First Federal's request for fees. In recommending the fee deletion, the referee stated that the "primary focus here are the fees sought for the Motion for Reconsideration after the Fair Market Value hearing, the redactions by [First Federal] of information re certain services rendered on grounds of attorney-client privilege or work product, unlawful detainer and wrongful eviction matters, and some of the time charged relating to redemption issues."

After a hearing on First Federal's motion for attorneys' fees, the court (Judge Collins) determined that the attorneys' fees were as calculated by the referee, \$151,296.90,

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<sup>6</sup> Blanchard argued First Federal could not collect fees for unsuccessful motions (\$67,952.50), unidentified or redacted fee entries (\$11,225), fees incurred after Blanchard offered First Federal a deed to the property in lieu of foreclosure (\$193,379.41), fees for preparing and defending its cost bill, including discovery (\$64,259.50), excessive, unreasonable or unnecessary fees through the end of 1996 (\$19,323.50), and questionable costs (\$17,563.31).

and that Blanchard was entitled to an offset of \$12,791.11.<sup>7</sup> The court thus entered judgment in First Federal's favor in the sum of \$81,477.51, the difference between the outstanding debt at the time of sale (\$757,971.72) plus attorneys' fees (\$151,296.90) less the \$12,791.11 offset, and the fair value of \$815,000.

This appeal followed.<sup>8</sup>

## DISCUSSION

Blanchard argues that, in order to prevent grasping lenders from misusing judicial foreclosure proceedings, this court should conclude as a matter of law that the debtor is the prevailing party, for purposes of an attorneys' fees award under Civil Code section 1717, when the lender fails to prove a deficiency at the fair value hearing.<sup>9</sup> He contends there was no deficiency because the value of the property exceeded the amount of the debt—"excluding costs and attorneys' fees"—at the time of the sale. He also argues the trial court overlooked equitable considerations in finding First Federal was the prevailing party, including the fact that Blanchard offered First Federal a deed in lieu of foreclosure to avoid litigation.

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<sup>7</sup> The offset was the amount of fees and costs Blanchard incurred in responding to First Federal's appeal of the court's non-appealable order at the fair value hearing in September 1996.

<sup>8</sup> First Federal filed an appeal, and Blanchard cross-appealed. First Federal did not pursue its appeal.

<sup>9</sup> Section 1717 provides in part:

“(a) In any action on a contract, where the contract specifically provides that attorney's fees and costs, which are incurred to enforce that contract, shall be awarded either to one of the parties or to the prevailing party, then the party who is determined to be the party prevailing on the contract, whether he or she is the party specified in the contract or not, shall be entitled to reasonable attorney's fees in addition to other costs.

...

Reasonable attorney's fees shall be fixed by the court, and shall be an element of the costs of suit.” (Civ. Code § 1717, subd. (a).)

We conclude there was no error in the award of attorneys' fees to First Federal.

**1. Blanchard's claim that he avoided a deficiency at the fair value hearing, and was therefore entitled to a favorable judgment, is without merit.**

Blanchard argues he was the prevailing party, because the value of the property (\$815,000) exceeded the amount of his indebtedness (\$757,971.72, exclusive of attorneys' fees and costs) as of the date of the sale. Therefore, he contends, First Federal was not entitled to a deficiency judgment. Instead, Blanchard claims *he* was entitled to judgment, and the trial court erred by failing to enter judgment in his favor at the time of the fair value hearing. Blanchard's argument, however, depends on the erroneous assertion that attorneys' fees and costs are excluded from the debt for purposes of calculating the deficiency. We disagree with that assertion, which misapprehends statutory requirements and overlooks the terms of the loan documents.

No authority in statute or case law stands for the proposition that costs and attorneys' fees should be excluded from the amount of indebtedness at the time of the sale for purposes of calculating a deficiency. The governing statutory provision itself suggests otherwise:

“... [A]fter [the fair value] hearing ..., the court shall render a money judgment against [the debtor] for the amount by which the amount of the indebtedness ***with interest and costs of levy and sale and of action*** exceeds the fair value of the real property ... sold as of the date of sale.” (Code Civ. Proc. § 726, subd. (b) [emphasis added].)<sup>10</sup>

Plainly, the deficiency calculation is to include “costs of levy and sale ***and of action*** ... [emphasis added].”<sup>11</sup> The statutory inclusion of “costs ... of action” with the amount of

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<sup>10</sup> Other language in section 726 describing requirements for a foreclosure decree similarly refers to a judgment “for any deficiency there may be between the sale price and the amount due with costs ...” (Code Civ. Proc. § 726, subd. (b).)

<sup>11</sup> Blanchard points to the succeeding language in section 726, subdivision (b), as support for his contention that judgment must immediately be entered after the fair value hearing, and that the question of fees must be determined on a post-judgment motion. The provision continues:



the indebtedness, we conclude, necessarily refers to the costs of the lawsuit that is a requisite part of the judicial foreclosure process. Blanchard does not suggest any other conceivable meaning for the term. And, under Civil Code section 1717, on which Blanchard relies, “[r]easonable attorney’s fees ... shall be an element of the costs of suit.” (Civ. Code § 1717, subd. (a).) Accordingly, attorneys’ fees and costs in the judicial foreclosure proceeding are “costs ... of action,” included by statute in the calculation of the deficiency: “the amount by which ... the indebtedness with interest and costs of levy and sale and of action exceeds the fair value of the real property ... sold as of the date of sale.”

Moreover, under the terms of the deed of trust itself, Blanchard’s indebtedness as of the date of the sale included attorneys’ fees disbursed “to protect Lender’s interest ....” Any such amounts became “additional indebtedness of Borrower secured by this Deed of Trust.” The trial court properly observed, at the hearing on First Federal’s motion for reconsideration, that First Federal’s reasonable attorneys’ fees and costs would be added to the arrearage, “and, taken together, we’ll know whether or not there’s a deficiency when applied against \$815,000.” Any other conclusion would amount to re-writing both the statute and the parties’ written agreements.<sup>12</sup>

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“In no event shall the amount of the judgment, exclusive of interest from the date of sale and of costs exceed the difference between the amount for which the real property ... was sold and the entire amount of the indebtedness secured by the mortgage and deed of trust.”

We see nothing in that sentence to support Blanchard’s contention. The quoted language does not state that the deficiency judgment may not include interest and costs. It merely indicates that the judgment, *exclusive* of those interests and costs, may not be greater than the difference between the sale price and the secured indebtedness.

<sup>12</sup> Blanchard also cites Bernhardt’s treatise on mortgage and deed of trust practice for the proposition that judgment should have been entered in favor of Blanchard at the time of the fair value hearing. But Bernhardt merely describes the procedures under section 726, and indeed specifically states that interest and costs are to be added to the indebtedness for purposes of calculating the deficiency. His entire comment is as follows: “After the hearing to adjudicate the fair value of the property on the date of sale, the court enters judgment. If a deficiency is established, a conventional money judgment in the plaintiff’s favor is entered for the difference between the indebtedness (plus interest and costs) and the fair value of the

Accordingly, Blanchard's repeated claim that he "avoided a deficiency" at the fair value hearing, and was therefore entitled to a favorable judgment, is without merit. The court did not find there was "no deficiency," nor should it have done so. The court correctly awaited the necessary information on reasonable attorneys' fees and costs, so that the deficiency, or lack thereof, could be determined.<sup>13</sup> In this case, the "indebtedness with interest and costs of levy and sale" (\$757,971.72), plus the "costs ... of action" as determined by the trial court (\$151,296.90), clearly exceed the fair value of the property (\$815,000).<sup>14</sup>

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property (as determined by the court), unless the sale price was greater than that value. CCP § 726(b). If the court finds no deficiency, it enters judgment in the defendant's favor." (Bernhardt, Cal. Mortgage and Deed of Trust Practice (Cont.Ed.Bar 3d ed. 2001) § 3.83, p. 187.)

<sup>13</sup> Blanchard's citation of precedent for the proposition that the prevailing party is the one who succeeds in the main objective of the litigation is similarly unavailing. The principle is correct; however, the assertions on which it is based – that Blanchard achieved his objective by "avoiding a deficiency" and that First Federal failed in its objective because it "did not obtain a deficiency at the time of the fair value hearing" – are flawed for the reasons discussed in the text.

<sup>14</sup> In his reply brief, Blanchard argues that attorneys' fees and costs incurred subsequent to the date of sale (June 12, 1996) should not be included in the deficiency calculation. If all fees subsequent to the date of sale are excluded, he contends, the debt plus attorneys' fees and costs to that date did not exceed the fair value of the property. Blanchard did not raise this argument in his opening brief, except by way of footnote. In any event, we are aware of no authority suggesting that costs incurred by the lender after a judicial foreclosure sale, to ascertain the fair value and the amount of any deficiency, are not recoverable. Blanchard cites *Penziner v. West American Finance Co.* (1937) 10 Cal.2d 160, but *Penziner* involved attorneys' fees incurred after a trustee's sale, to defend against third party suits to foreclose on mechanics' liens against the property. The Court merely held that attorneys' fees and costs incurred after a trustee's sale were not payable out of the proceeds of the sale, because the purchaser at such a sale takes the property subject to all liens against it. (10 Cal.2d at p. 180.) In this case, a deficiency would exist even if the court considered only attorneys' fees incurred through October 1996 (when First Federal's motion for reconsideration of the court's fair value ruling was denied), and even if the entire amount of fees ultimately disallowed (which included fees for the reconsideration motion) were deducted from that sum.

**2. Blanchard's arguments that equitable considerations and public policy mandate he be considered the prevailing party are likewise without merit.**

Blanchard argues in substance that First Federal pursued the predatory objective of obtaining a large deficiency judgment by making an unrealistically low credit bid, almost one-third less than the property's fair value, after which the bank could then obtain a double recovery by selling the property for its fair value or more. Blanchard asserts he prevented that double recovery by his successful defense at the fair value hearing, where the court accepted his \$815,000 appraisal over the bank's faulty \$560,000 appraisal. Therefore, he, not First Federal, is entitled to receive a fee award, or otherwise similar misconduct by lenders and their lawyers would become routine.

Again, we disagree. The "double recovery" Blanchard posits may be theoretically possible, if a debtor fails to contest an unreasonably low appraisal at the fair value hearing. However, the Legislature has established the requirements and procedures for judicial foreclosure, including the protections available to the debtor. The fair value provision limiting the size of the deficiency is one of those protections, and the debtor's right to redeem the property from the buyer at the foreclosure sale for the sale price—as Blanchard did here—is another. This court is not at liberty to add to those statutory protections under the guise of public policy – particularly by concluding, contrary to the terms of section 726 and the parties' loan documents, that attorneys' fees and costs are excluded from deficiency calculations.

Blanchard argues that First Federal could have achieved all its objectives, other than a deficiency, by conducting a private sale, or by accepting his offer of a deed in lieu of foreclosure. However, First Federal had the statutory right to seek a deficiency, and it is only with benefit of hindsight that its choice of remedies may appear debatable. First Federal succeeded, over Blanchard's opposition, in obtaining a decree of foreclosure and establishing Blanchard's liability for any deficiency that might arise from an insufficient sale price. First Federal was contractually entitled to the fees it incurred in doing so. And the fact remains that there was a deficiency. The inclusion of attorneys' fees in the

deficiency calculation does not mean, as Blanchard suggests, that First Federal could “continue to add attorneys’ fees to the amount of the debt indefinitely and at its discretion after the sale,” in order to “manufacture a deficiency.” The debtor is fully protected by the requirement that fees must be reasonable, and are fixed by the court.

**DISPOSITION**

The judgment is affirmed. First Federal is to recover its costs on appeal.

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BOLAND, J.\*

We concur:

LILLIE, P.J.

WOODS, J.

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\* Judge of the Los Angeles Superior Court, assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.